Stewardship
Active generosity

What to do with your church reserves fund

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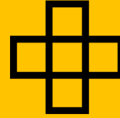

About Stewardship

Stewardship is here to help the Christian community in the UK to give and receive.

We help over 30,000 people to give generously and sacrificially to support the causes they love, and connect them in to a growing community of 4,000 churches, 6,000 charities and 2,800 individual partners creating positive change, and being responsible stewards, in Jesus' name.

For more than a century we have actively served those pioneering Christian mission. Together, we are driven by our desire that the wider world will encounter Jesus through the generosity of his people and the transformational work of the causes they support.

We call this **Active Generosity**.

1 Introduction

Often churches have great systems in place for handling smaller amounts of money on a day-to-day basis but struggle far more when considering:

- Whether to hold reserves or surplus funds;
- How to calculate levels of reserves;
- How to look after and invest any surplus funds that they may have.

This and an accompanying paper How to set a church reserves policy offer churches both a Biblical and practical perspective on how to think about reserves and then what to do with them. The 'How to set a church resources policy' paper considers the first two issues, whereas this paper focuses on the third question of how to look after or invest surplus reserves.

Stewardship is **not authorised to give investment advice**, and neither does it have the necessary expertise to do so. As such, this paper is designed to inform trustees of the types of investment that might be available recognising that expert advice should be sought where churches intend to invest in anything more complex than bank time deposit accounts. **Nothing** in this paper should be considered to constitute investment advice.

Different churches place the responsibility of looking after its finances with different people - church leaders, trustees, elders, pastors - but for the purpose of this paper we'll refer to the 'leadership team' as the decision-making group.

2 Where should we keep our reserves?

The accompanying paper ('How to set a church reserves policy') introduced the concept of different types of reserves:

- Running reserves: money placed on one side to cover ongoing church costs in the event of a loss of income or an increase in running expenses and;
- Project reserves: money set aside for a specific future project;
- Unforeseen events reserves: money put aside to safeguard against unforeseen or unknown future events.

As these reserves are held for very different reasons, there will be an impact on where and how they should be held.

Running reserves could be called on at any time and at relatively short notice. As such they need to be predictable in value (not fluctuating unduly) and 'liquid' (available at short notice). Running reserves funds will generally be kept on deposit at a bank.

Project and unforeseen event reserves can sometimes be invested differently (depending on other factors examined below). For smaller amounts a simple deposit account is all that is needed. Whilst the interest rate may not be high, the interest won't be taxed and generally balances up to £85,000 are covered by the Financial Services Compensation Scheme (FSCS) for each banking group[1] with which you invest.

For larger amounts you can branch into other forms of deposit account.

Here is a helpful simple Sequential Step Strategy (SSS) to illustrate a way of working out how much of your surplus to keep on one side and where to keep it:

Step 1

Ensure that you have paid off any debts (apart from a mortgage) – loans, outstanding bills etc.

[1] Some banks may be in the same banking group which means that a single balance of £85,000 applies to all funds in that group rather than to each balance. Further information can be found at www.FSCS.org.uk

Step 2

Build up sufficient surplus so that your day-to-day bank account balance stays above an amount equal to a full month's normal spending. For example, if your church normally spends £10,000 per month (on everything) then aim for the current account not to drop below £10,000.

Step 3

Invest the equivalent of the remaining balance of your agreed running reserves in a deposit account with immediate access. A simple deposit account with your bank would normally be sufficient. For example:

- A church with a monthly spend of £3,000 and a running reserves policy of holding an amount equal to three months' expenditure (£9,000) should aim to be able to put aside an additional £6,000 on top of the £3,000 already held in step 2. (ie £9,000 in running reserves, with £3,000 in the current account and £6,000 in the deposit account.)
- A church with a monthly spend of £3,000 and a running reserves policy of holding £25,000 (perhaps due to lease commitments or other conditions) would aim to put aside an additional £22,000 on top of the £3,000 already held in Step 2. (ie £25,000 in running reserves, with £3,000 in the current account and £22,000 in the deposit account.)

Step 4

If your board wishes to keep higher levels of reserves or have reserves set aside for particular projects or to safeguard against anticipated or unexpected events, then you could consider investing those funds in term/time deposits or notice accounts where you would normally give notice on withdrawing the funds or have periodic opportunities to take the money out.

These accounts will sometimes incur penalties if funds are withdrawn before the end of the term or outside of the periodic withdrawal periods, but they will usually pay a higher rate of interest.

3 Should reserves only be invested in deposit or notice accounts?

Running reserves and reserves held to protect against unforeseen events may be called on at relatively short notice. The recent pandemic has provided a real-life example of an unforeseen event having a significantly adverse impact on the finances of many churches and charities. Therefore, it is generally appropriate for them to be invested in deposit or notice accounts where the amount available is known, guaranteed and fully accessible at short notice.

Reserves held for a particular project may have a longer life span, so the term of the savings should match the term of the project.

If a church has additional funds which it wishes to put on one side for a longer period of time - whether for a particular purpose in the future or because they are not ready to use the surplus yet - there is an argument for placing the money in other forms of investment.

Case study

A board (Church C) with whom I was talking had carefully saved £800,000 in order to be ready to put in an offer when a suitable building became available. However, it had dawned on them that, being based in London, they may never be able to afford a building. But neither did they feel that the church needed to spend significant amounts of money in the immediate future.

They were uncomfortable with having quite so much in reserves. Should they give it away, should they spend it, should they invest a little more aggressively or should they invest in social impact investments in order to make the money do something?

As soon as alternatives to simple bank accounts are considered, the board should develop policies, both for their approach to financial risk and for ethical or responsible investment, and consider whether professional advice is required.

4 How much risk should we take (if any) with the reserves?

In investment there is generally a trade-off between risk and return. If you are willing to take a higher risk with your investment you have the opportunity to enjoy a higher potential return. If you wish to reduce risk (it isn't possible to avoid all risk) then as a result, you will have to accept lower investment income and growth.

In order to work out a church's 'risk profile', four factors should be examined:

1. Risk tolerance (the attitude toward taking risks)	The risk profile of a 'church' is primarily driven by the attitude of the leadership team toward taking risks - their risk tolerance. It is likely that the church's attitude to risk in its life and ministry will be reflected in its attitude to risk in the financial and investment dimensions too.
2. Capacity for loss (the ability to take risk given your goals)	Until the church has covered the 4 steps of the SSS above, there is unlikely to be a capacity to absorb a loss. On the other hand, a church which carries reserves equal to one year's expenditure could, for example, cope with a fall of 10% in its investments without a devastating impact on its activities or goals, so it has a higher capacity for loss.
3. Risk requirement (the need to take risk given your objectives)	A high financial requirement might require a high return and therefore may require a higher risk in investment. This is rarely the case for a church or a charity. Faced with a high-risk requirement, a board is more likely to change its goals and targets to something achievable with less risk.
4. Risk time-frame (for how long are you able to invest)	A long timescale allows for investments to recover when values have fallen. So the longer the time frame, the higher the risk that can be accommodated. A church's time frame is predominantly short. However, if the four steps of the SSS have been completed, a longer time frame is possible. For example, having moved through the four steps, a leadership team decides to plan to buy a building in 5 or 10 years' time, or set up a fund to provide an income for the next 20 years.

In our experience, the combination of these four factors with the church's default attitude to risk will usually result in a risk profile which would be defined as 'low' or 'cautious'.

Case study (continued)

Church C had covered the first four steps of the 'SSS': no debt; cash in the current account to pay the next month's bills; more than three months' costs on deposit; and a surplus of £800,000 put aside for a future building project.

So, to gauge their risk profile we examine the four risk factors:

1. They are somewhat 'risk-taking' by nature, trying new projects, expressing high levels of faith in some of their ministry decision-making. A certain amount of 'risk tolerance';
2. They had 'capacity for loss' in that if their £800,000 had fallen in value to, say, £750,000, they may not have been happy but it wouldn't have stopped them doing what they do;
3. They wanted to buy in London, which would cost quite a lot of money, and therefore it would be good if their investments earned a better return than the low bank deposit rates currently on offer. That way they might have more funds available when needed in the future. So their 'risk requirement' was higher;
4. They were willing to take a five-year (or longer) view so the 'risk time-frame' wasn't short.

In the end, Church C might conclude that, on balance, their overall risk profile is moderate. They would ensure that SSS steps 1-4 were covered so that they didn't have to take a 'no risk' approach to their surplus. Or they may just give the surplus away! Or they may accelerate some of the ministry ideas and use the money sooner.

5 How do we invest in a way that matches our risk profile?

These are three common forms of saving and investment:

Bank and deposit accounts

So long as balances are kept below the FSCS threshold (currently £85,000)[2] (see 2 above), these carry very little risk to capital. In other words, you should be able to rely on getting back out what you originally put in. However, if interest rates run below general inflation (or below the rise in cost of the specific item the church is seeking to acquire) then the value of the deposit in real terms may be eroded. In other words, its spending power will be reduced over time.

Time/term deposits or notice accounts

Falling within the same FSCS guarantee scheme, these also carry very little risk to capital. In exchange for leaving the money with a bank for an agreed period, you can often earn a little extra interest. You need to ensure that you won't need to call on the money before the end of the term or notice period (which can be anywhere from a few weeks to several years). Generally speaking, the longer you tie the money up, the higher the rate of interest.

Mutual funds

These take your investment and accumulate it with many other investors to create a large pool of money - usually called a 'fund' (unit trusts, OEICs etc). A fund manager will then use their investment expertise; their capacity to buy in bulk and their ability to diversify their investments in a range of underlying investments (often company bonds and shares) in an attempt to earn a higher return than a bank deposit.

Mutual funds cover a wide range of risks. You can choose very low risk ones, very high risk ones and anything in between. You can choose one that invests primarily in property if you wish to correlate (match) your returns with your goals (e.g. buying a property) or ones that have an ethical bias (see 6 below).

Unless you have expertise on the board, it will be necessary to take expert advice on how to build up a portfolio that both matches your risk and is cost effective. Stewardship does not have that level of expertise and as such is not authorised to give investment advice. Any such investment should be reviewed regularly (preferably annually).

[2] This threshold changes from time to time, so please research the current level before investing.

Should we invest "ethically" or "responsibly"? The 'Wonga' question

In 2013, the Archbishop of Canterbury was caught on the hop by the disclosure that the Church of England had investments (albeit a tiny amount) in Wonga, a notorious payday loan company. This clashed with the message he was trying to send criticising the levels of interest charged by such lenders.

In the past the question of responsible investment was sometimes presented as a binary choice between investing ethically in order to do the right thing with the money (in this case to avoid Wonga) and investing 'non-ethically' in order to obtain the best possible returns for the church's funds (thereby making all investments acceptable). It is now generally understood that investment returns need not be sacrificed when an ethical or responsible investment strategy is pursued.

Ethics is more of an art or a philosophical process than an exact science when it comes to investment and as such there is no complete and definitive list of companies which may be described as ethical or operating responsibly. Often larger companies (those typically included in many mutual fund portfolios) are involved in a range of different types of business that may not all be considered as being equally ethical. Take for example a pharmaceutical company researching drugs to combat malaria, as well as undertaking stem cell research with the potential for 'designer' babies.

As with risk, a church will have to determine its attitude toward responsible investment. Its practice, or the way it operates, will often reflect any underlying ethical values. For example, does it have an equal opportunities employment policy? Is the coffee bought from a Fair Trade outlet and does it discourage single-use plastics? Does the church encourage walking to church or using public transport as an alternative to using private vehicles? Have they fitted solar panels? If there is an ethical attitude expressed in these things, then consistency would seem to demand that the church invests its money in a similar way.

In April 2022, Judge Butler-Schloss handed down a judgement which said, "where trustees are of the reasonable view that particular investments or classes of investments potentially conflict with the charitable purposes, the trustees have a discretion as to whether to exclude such investments and they should exercise that discretion by reasonably balancing all relevant factors including, in particular, the likelihood and seriousness of the potential conflict and the likelihood and seriousness of any potential financial effect from the exclusion of such investments."

The Charity Commission advises, "Consider whether it would be in the interests of the charity to adopt an ethical approach. They might want to avoid investments that conflict in a practical way

with the aims of the charity or that might alienate donors or beneficiaries, or they might want to make investments that reflect its values and ethos"[3].

The board should answer this question first: Are we an ethically-orientated organisation and, if so, should our investment policy reflect this?

How do we invest responsibly and ethically?

In 1984, Friends Provident Insurance company (now swallowed up into Aviva) launched the Stewardship Fund (no relation) as a pooled investment available as a unit trust or through an insurance bond. The Stewardship Fund was a screened ethical fund meaning that it excluded companies from its potential pool of investment if they breached certain ethical criteria (such as earning returns from tobacco, alcohol, pornography, armaments etc).

Since then, the market has expanded considerably, with a wide range of investment options available and a demonstrable positive track record for good investment returns.

7.1 Approaches toward responsible investment

This sector of the investment market is generally given the title "Responsible Investment" and can be described loosely as lying along a spectrum ranging from:

A – the avoidance of harm

B – seeking to benefit all stakeholders

C – making a contribution to solutions

As a "responsible" investment mandate develops from simple avoidance of harm toward making a contribution, i.e. making an impact, a popular measure of effectiveness is through the United Nations Sustainable Development Goals:

https://www.un.org/sustainabledevelopment/news/communications-material/

Responsible Investment does not have to be limited to mutual funds. A church could apply an ethical strategy to most parts of its financial arrangements:

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[3] wwww.gov.uk/government/publications/managing-charity-assets-and-resources-cc25/managing-charity-assets-and-resources#investing-charitable-funds

- Bank Accounts (e.g. Co-op Bank, Triodos Bank or local Credit Unions) which have a policy of ethically screening the loans they make to companies;
- Investment funds: unit trusts, Oeics, Sicavs, investment trusts;
- Corporate Bonds: fixed-term loans to socially responsible companies;
- Shares and other direct investment in socially responsible companies, social enterprises and not-for-profit organisations with a social benefit;
- Community Investor Accounts: limited availability UK investments designed to benefit communities (this type of investment has been offered for example by Triodos Bank);
- Micro-credit accounts (e.g. shared interest accounts) designed to provide a fair source of finance to people in developing countries;
- Specialist managed portfolios for larger amounts, typically more than £200,000, using ethical criteria dictated by the board;
- Social Impact Funds which aim to give a social return as well as a financial one.

This is a specialist, but increasingly important, area for churches with surplus reserves to understand and profession help is **strongly** recommended.

7.2 Investment returns

Responsible funds are usually expected to be more volatile (they tend to fluctuate more in value) than their mainstream equivalents. At times they can out-perform; at other times they can fall further behind their peers. There are periods in the investment cycle when certain non-ethical shares do particularly well - tobacco, alcohol and armaments being the obvious ones. Then again, there are periods when the more speculative and forward-looking funds come good. Over the long term, many ethical funds have produced very good returns.

7.3 Risk

Since responsible investment, by definition, reduces the number of shares, securities or funds in which you can invest, it tends to increase the volatility (the fluctuation in value) of your portfolio and therefore the risk profile. This risk can be mitigated by spreading the available funds between different asset classes as you would do with a non-ethical investment portfolio.

It is possible to have an ethical investment policy with lower risk investments (e.g. bonds and cash) as well as higher risk (e.g. shares and social impact investment).

7.4 Costs

It costs more to run an responsible fund since, in addition to the usual investment disciplines of selecting stocks and shares, the management team have to apply further expertise (and systems) in order to perform the necessary screening. This is usually reflected in a small additional management charge, which lowers the overall investment return.

Investment decision-making

Who makes the decisions and who holds the decision-makers to account? This will depend on the different governance structures for each church. Although the 'leadership team' may make the formal decision and take responsibility for it, it is usually good practice to have external expertise contribute specialist advice, especially where more complex investments are being contemplated.

Decision 1

Decide whether to adopt a Sequential Step Strategy for your reserves as described in (2) above. If not, consider alternatives.

Decision 2

How much do you wish to retain in running reserves and what are the main conditions that influence this decision? For more on this see our associated briefing paper How to set a church reserves policy.

Decision 3

If you have more funds than needed for (1) and (2), decide whether to give it away; accelerate spending; consider new forms of ministry; save for the future (project reserves) or a combination.

At this point, it would normally be recommended to retain the services of a specialist investment adviser, particularly if you wish to establish a responsible investment policy or have substantial funds to invest.

Decision 4

If saving for the future: what is the time frame, the purpose, and the return requirement? For example, "We will invest this money for a minimum of five years with the aim of growing a building fund and we wish to invest for capital growth".

Decision 5

Consider the risk questions in 4 above and decide on your risk profile.

Decision 6

Consider the ethical options in section 6 above and decide on which approach you wish to take.

Decision 7

Choose and instruct an adviser to implement this strategy for you. If you do not have sufficient expertise within the board, bring in a specialist to assist you with decisions 4, 5, & 6.

An annual review

If you are running with surplus funds, place an annual item on your agenda which covers a review of:

- The decision to have surplus reserves;
- The purpose and time frame;
- Your risk profile (which should change only very rarely);
- Your ethical policy;
- Investment performance and overall returns (including non-financial ones, if relevant).

The leadership team should formally record whether or not there are any changes to the approach you are taking to the investment of surplus funds. A statement to that effect would go in the Annual Report.

Conclusions

For most churches, most of the time, investment decisions are unlikely to be more complex than determining the appropriate time horizon for money deposited in a time deposit bank account. It is only in cases where churches are saving for significant projects or have accumulated a significant level of reserves that more complex investment options might be required.

Where this is the case, it is strongly recommended that the leadership team seeks a properly qualified adviser to help them. Investments in shares, bonds, mutual funds etc., all carry a more significant level of risk and the leadership need to understand that risk and the consequences associated with it before investing in this way.